

DEPARTMENT OF STATE REVENUE

**SUPPLEMENTAL LETTER OF FINDINGS NUMBER 96-0590 FIT
Financial Institutions Tax
For Tax Periods: 1992 Through 1994**

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning specific issues.

ISSUES

**I. Financial Institutions Tax: Mortgage Backed Securities
Authority: IC 6-5.5-4-4-IC 6-5.5-4-13.**

Taxpayer protests the assessment of tax on mortgage backed securities.

STATEMENT OF FACTS

Taxpayer was originally organized as a non-Indiana state chartered savings and loan association in 1889, converted to a federally chartered savings and loan association in 1981 and converted to a federally chartered savings bank in 1991. Taxpayer is a wholly owned first tier subsidiary of another foreign corporation. Taxpayer is regulated by the Director of the Office of Thrift Supervision and the Federal Deposit Insurance Corporation which, through the Savings Association Insurance Fund and the Bank Insurance Fund, insures the deposit accounts of Taxpayer. Taxpayer is further subject to regulations of the Board of Governors of the Federal Reserve System with respect to reserves required to be maintained against deposits. On February 26, 1993, the parent corporation's three FDIC insured federal savings banks, Taxpayer and its wholly owned subsidiaries and two other federal savings and loan associations merged into a single federal savings bank that operates as Taxpayer. The Department audited Taxpayer for the years 1992, 1993 and 1994. The audit includes on a unitary basis the total income of the

Holding Company parent along with all subsidiary corporations. The audit resulted in an additional financial institutions tax assessment for those years. Taxpayer timely protested the assessment. After a hearing and issuance of a Letter of Findings, Taxpayer requested a rehearing. Further facts will be provided as necessary.

DISCUSSION

FINANCIAL INSTITUTIONS TAX: MORTGAGE BACKED SECURITIES

Taxpayer protests the inclusion of income from mortgage backed securities in the receipts attributable to Indiana in the apportionment factor. It receives interest from the company that issues the security. IC 6-5.5-4-4 through IC 6-5.5-4-13 enumerate the receipts that must be included to determine which receipts are attributable to transacting business in Indiana. Mortgage backed securities are not included in that listing. Therefore, Indiana can only impose financial institutions tax on the income from mortgage backed securities which have nexus with Indiana. Taxpayer owns mortgage backed securities that are issued mostly by FNMA, FHLMC and some private issuers. Taxpayer does not own the underlying loan, nor does it receive interest on the loan from the borrower. Taxpayer has no interest in the real estate backing the underlying mortgages. These mortgage backed securities do not have sufficient connection and should not be included in the apportionment factor.

FINDING

Taxpayer's protest is sustained.